

Kitimat Poised to See Resurgence in Exports

By Dan Schrier

Kitimat, a town with a population of around 9,100 located in B.C.'s northwest, has long punched above its weight in terms of being a source for exports from the province. Since its inception Kitimat has been home to the Alcan Smelter (now Rio Tinto Alcan), a major aluminum producer. Until recently, it was also the location of a large pulp and paper mill and it once housed a methanol plant as well. In its peak years, close to \$1 billion worth of merchandise exports were shipped through the Port of Kitimat.

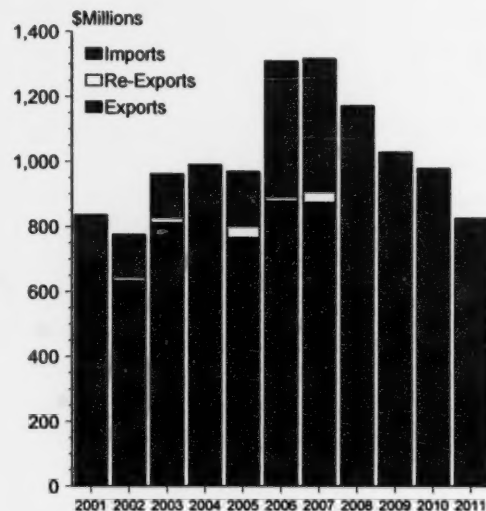
However, the Methanex methanol and ammonia plant was permanently closed in 2005 and the Eurocan pulp and paper mill shut down for good in January 2010. The closure of the pulp and paper mill in particular was a large blow for the municipality as over 500 jobs were lost to the community.

The volume of goods shipped through the Port of Kitimat has slumped over the last four years, first as a consequence of the global economic downturn, which affected demand for the goods produced in Kitimat and more recently, due to the shutdown of the pulp and paper mill and the closure of two pot lines in the aluminum smelter in preparation for modernization of the plant.

While the closures of the Methanex plant and the Eurocan mill have been tough for Kitimat, their former sites could play a major role in Kitimat's resurgence. The Eurocan site has been purchased by a partnership comprised of Apache Canada Ltd., EOG Resources Canada Inc., and Encana Corporation who together

own Kitimat LNG, which plans to build a liquefied natural gas (LNG) facility on the Haisla First Nation's land adjacent to Kitimat. The Eurocan site is expected to be used as a staging area, with a workers' camp and an area for loading and unloading materials to be used in the construction of the liquefaction plant. The former Methanex site was purchased by Royal Dutch Shell, which plans to build yet another LNG plant on the site.

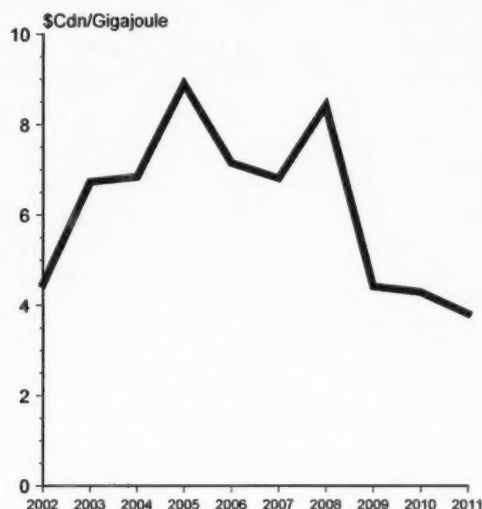
The value of goods exported from the Port of Kitimat has fallen the last four years



Source: Statistics Canada

The Kitimat LNG project is expected to begin construction in 2012 and has already received approval from the National Energy Board to export LNG. The plant is expected to be operational by 2015, with an initial annual production of five million tonnes and plans to eventually double that. The primary market for the LNG will be Asia, where prices for LNG are far higher compared to those in North America.

The price of exported natural gas has slumped in recent years with growth in supply



Source: National Energy Board

Natural gas prices in North America spiked in 2005 when hurricanes Rita and Katrina disrupted the supply from the U.S. Gulf of Mexico, then fell for a couple of years before jumping again in 2008 when record oil prices created demand for alternative energy supplies. In more recent years, the price of natural gas has dropped significantly as new discoveries have increased the North American supply of gas and created somewhat of a glut on the market.

In particular, major discoveries of shale gas reserves, such as the one in the Horn River Basin in Northeast British Columbia, combined with technological improvements in extraction methods that have made it more economical to extract shale gas, have boosted the supply of gas in North America such that it exceeds demand. Normally, an excess domestic supply, combined with demand elsewhere, would result in the product being exported; however, in order for natural gas to be shipped overseas it must first be liquefied. Currently there is only

one natural gas liquefaction facility in North America. The Kenai LNG plant in Alaska was scheduled to terminate operations at the end of December 2011, but it appears it may resume shipments in 2012. Regardless of whether or not the plant does resume operation, it is much smaller in scale than the one planned by Kitimat LNG and is nowhere near large enough to deal with the large volume of potential exports.

The dearth of gas liquefaction facilities in North America coupled with the bountiful supply of gas served as the impetus for the development of an LNG export facility in Kitimat. However, the Kitimat LNG project isn't the only LNG facility planned for Kitimat. As noted above, Shell is also planning to build an LNG plant and there is also a third project planned for the area.

The Shell project as planned could be even larger than the Kitimat LNG facility. The purchase of the vacated industrial site in Kitimat is a good indication that Shell and its partners are serious about proceeding with the project. Just last month, it was announced that PetroChina Co. Ltd. has committed to partner with Shell in a shale gas operation in B.C., which should reduce Shell's development costs and makes it that more likely that the Kitimat facility will proceed.

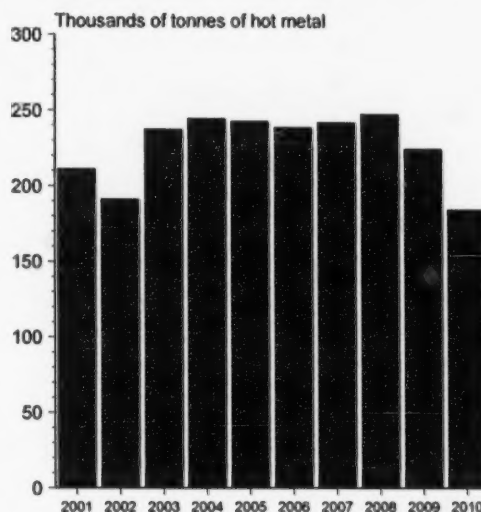
The third proposed LNG plant by the Douglas Channel Energy Partnership would be a small-scale floating terminal on the Douglas Channel within the District of Kitimat and the Haisla Nation territory. Initial production would be 700,000 tonnes per year, increasing to 900,000 tonnes. The National Energy Board has approved the company's application for an export license and the expectation is that production of LNG could start early in 2014.

While Kitimat appears poised to become a hub for LNG production, those are not the only major projects potentially on the horizon for the community. For example, there is the much publicized proposal by Enbridge Inc. to construct a pipeline from Alberta to Kitimat and to build a marine terminal in Kitimat for the export of oil to Asia. Unlike the LNG projects, which have generally been positively received, the Enbridge Northern Gateway Pipeline proposal has garnered a great deal of protest, with opinion, even in Kitimat, split between those who see it as a huge economic opportunity and those who believe it poses too much of a risk to the environment. The proposal will have to clear a number of hurdles including an environmental review process if it is to proceed.

In addition to the potential of new industry being developed in Kitimat, there has also been positive news with regard to the main industry currently operating in the municipality, the Rio Tinto Alcan aluminum smelter. After years of delays, it appears that the company is ready to proceed with modernization of the existing smelter. The project will boost the smelter's current production capacity from around 282,000 tonnes per year to approximately 420,000 tonnes annually. While there will be a reduction in employment associated with the modernization due to gains in efficiency, it will ensure that the smelter remains operating well into the future, which will secure around 1,000 well-paying jobs in the community.

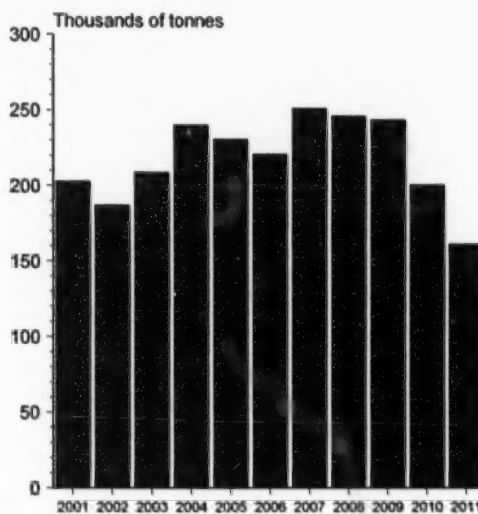
The project has already started with the decommissioning and demolition of two pot lines to make way for construction of the new facility. The closure of the lines is reflected in the drop in production at the smelter and also can be seen in the reduction in B.C.'s exports of unwrought aluminum over the last couple of years.

Production at the Kitimat Smelter dropped in 2010 as a result of the closure of two potlines in preparation for re-modernization



Source: Rio Tinto Alcan

The drop in production is mirrored by the dip in BC's exports of unwrought aluminum



Source: Statistics Canada

The Kitimat smelter has always had a competitive advantage due to the availability of inex-

pensive hydro power, but over the years that advantage has been eroded due to out of date smelting technology. With the modernization of the plant, the Kitimat smelter will become one of the most efficient and lowest-cost smelters in the world and will have the additional benefit of cutting greenhouse gas emissions approximately in half.¹

Once the modernized smelter is in full production, there should be a substantial increase in B.C.'s aluminum exports. The LNG facilities offer the potential for a major jump in exports as well, which puts Kitimat in a position of becoming one of the top exporting centres in the province. The Port of Kitimat is already the third largest in the province, behind only Port Metro Vancouver and the Port of Prince Rupert. The expansion in aluminum production and the possible addition of new industry in Kitimat and the surrounding area could herald a major resurgence in exports for the community and its port.

¹ Rio Tinto Alcan, "Rio Tinto Alcan Works Modernization."

<http://investnorthwestbc.ca/major-projects-and-investment-opportunities/map-view/kitimat/rio-tinto-alcan-kitimat-works-modernization>